Nos. 93-1612 and 93-1613

IN THE

Supreme Court of the United States

OCTOBER TERM, 1994

NATIONSBANK OF NORTH CAROLINA, N.A., *et al.*,
Petitioners,

v.

VARIABLE ANNUITY LIFE INSURANCE CO.,
Respondent.

EUGENE LUDWIG, COMPTROLLER OF THE CURRENCY, *et al.*,
Petitioners,

v.

VARIABLE ANNUITY LIFE INSURANCE CO.,
Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES
COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF OF THE NEW YORK CLEARING HOUSE ASSOCIATION AS *AMICUS CURIAE* IN SUPPORT OF PETITIONERS

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July 29, 1994

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Pursuant to Rule 37.3 of this Court, The New York Clearing House Association (the "Clearing House") respectfully submits this brief with the consent of all parties.

INTEREST OF *AMICUS CURIAE*

The Clearing House is an unincorporated association of eleven leading commercial banks in the City of New York.[1] Four of the Clearing House member banks are national banking associations subject to the National Bank Act (the "NBA")[2] and, thus, to the supervision and regulation of petitioners the Comptroller of the Currency and the Office of the Comptroller of the Currency (together, the "OCC"). The Clearing House often appears as an *amicus curiae* in cases, such as this, raising important questions of banking law.

The Clearing House has a substantial interest in the questions presented here because of its member banks' involvement in the brokerage of annuities, an important and growing part of commercial banking. In 1993, commercial banks, including Clearing House member banks, sold an estimated $16 billion worth of annuities, *see* Karen Talley, *Bank Annuity Sales Seen Surging in '93*, THE AMERICAN BANKER, June 30, 1993, at 17, and such sales represented approximately seven percent of all bank brokerage activity. *See* Kurt Cerulli & David Nadig, *Variable Annuities Add a Steady Flow to Bank Brokerages' Revenue Streams*, THE AMERICAN BANKER, July 14, 1993, at 12.

In addition, relying on the authorizations and regulations of the OCC and other bank regulators, Clearing House

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[1] The members of the Clearing House are The Bank of New York, The Chase Manhattan Bank, N.A., Citibank, N.A., Chemical Bank, Morgan Guaranty Trust Company of New York, Bankers Trust Company, Marine Midland Bank, United States Trust Company of New York, National Westminster Bank USA, European American Bank, and Republic National Bank of New York.

[2] Ch. 106, 13 Stat. 99 (1864) (codified, as amended, in sections of Title 12 of the United States Code).

member banks sell as agents other products related to the business of banking that, unlike annuities, are generally considered insurance. The sale of these products, which include credit life, credit disability, mortgage life, mortgage disability and involuntary unemployment insurance, provides millions of dollars in revenues to national banks each year.

More generally, the Fifth Circuit's crabbed construction of the "incidental powers" clause of Section 24 (Seventh) of the NBA calls into question the extent to which national banks may continue to respond, as they have for more than 100 years, to the rapidly evolving needs of their customers. The OCC has authorized national banks to engage in many activities, not specifically enumerated in the NBA, that are incidental to the "business of banking." If the NBA had to be amended every time national banks sought to offer new banking products or services, such banks could not compete successfully with other financial intermediaries, including savings banks, securities brokerage firms and mutual funds.

SUMMARY OF ARGUMENT

1. The Fifth Circuit flatly contravened the principle of judicial deference established by this Court in *Chevron U.S.A., Inc.* v. *Natural Resources Defense Council, Inc.*, 467 U.S. 837, 842-45 (1984) ("*Chevron*"), in not deferring to the OCC's determination that the brokerage of annuities by national banks is authorized under Sections 24 (Seventh) and 92 of the NBA. Congress did not clearly bar national banks from brokering annuities in the NBA, and interpretation of the statutory term "business of banking" in Section 24 (Seventh) requires the OCC's special expertise.

Indeed, the respective determinations by the New York Court of Appeals in *New York State Association of Life Underwriters, Inc.* v. *New York State Banking Department*, 83 N.Y.2d 353, 363-64, 632 N.E.2d 876, 881-82, 610 N.Y.S.2d 470, 475-76 (1994) ("*NYSALU*"), and by the Fifth Circuit judges who dissented from the denial of rehearing *en*

banc (24a-27a),[3] that annuities are not a form of insurance—but financial investment instruments of the sort that banks have long sold—demonstrate powerfully that the OCC had far more than a reasonable basis—all that was necessary under *Chevron*—for authorizing national banks to broker annuities.

The Fifth Circuit's failure to defer to the OCC's reasonable interpretation of the NBA threatens regulatory predictability and stability in the commercial banking industry. If national banks could not rely on OCC regulations under, and interpretations of, the NBA, they would be deprived of the predictability necessary for the development of innovative banking practices.

2. The Fifth Circuit's *de novo* determination that national banks may not act as agents for the sale of annuities rests on the mistaken proposition that annuities are a "'general' type of insurance" and not a financial investment instrument. (14a). From that premise, the court reached two erroneous conclusions: (i) that the sale of annuities as agent *is not* included in the express grant of authority in Section 24 (Seventh) for national banks to engage in all aspects of the "business of banking," and (ii) that such business *is* the sale of a form of general insurance that Section 92 limits to banks in towns of 5,000 or fewer inhabitants. (13a-17a).

a. The great weight of authority firmly establishes that annuities are financial investment instruments, and it is settled that banks may act as agents for the sale of securities, certificates of deposits and other financial investment instruments to their customers. The court below ignored this authority and relied, instead, on a mistaken conception of annuities and an unfounded—and, indeed, unarticulated—

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[3] Citations in the form "__a" are to the appendix to the petition for a writ of certiorari in No. 93-1612.

construction of national banks' power to conduct the "business of banking."

Both the language of, and decisions interpreting, the incidental powers clause support the OCC's determination that national banks are expressly authorized to engage in all aspects of the "business of banking." The brokerage of annuities is clearly part of the business of banking, because such brokerage (i) involves the financial intermediation that is the essence of banking, and (ii) is akin to the brokerage of securities expressly permitted by Section 24 (Seventh). Moreover, by increasing the availability of annuities and by allowing national banks to compete on an equal footing with state-chartered banks and other financial intermediaries in the growing annuities market, the OCC's determination promotes sound banking policy.

b. Even if annuities are considered "insurance" for purposes of Section 92, the NBA should not be construed to bar national banks located outside of small towns from brokering annuities and credit-related insurance products that are incidental to the business of banking. The statutory language and legislative history support the OCC's interpretation that Section 92 is a supplemental grant of authority for national banks located in small towns and does not otherwise restrict the "business of banking."

ARGUMENT

I. THE FIFTH CIRCUIT DIRECTLY CONTRAVENED *CHEVRON* IN OVERRIDING THE OCC'S REASONABLE DETERMINATION THAT NATIONAL BANKS MAY BROKER ANNUITIES.

This Court has "long recognized that considerable weight should be accorded to an [agency's] construction of a statutory scheme it is entrusted to administer." *Chevron*, 467 U.S. at 844. Such judicial deference is particularly appropriate where, as here, "[t]he subject under regulation is

technical and complex." *Aluminum Co. of Am.* v. *Central Lincoln Peoples' Util. Dist.*, 467 U.S. 380, 390 (1984); *see also Clarke* v. *Securities Indus. Ass'n*, 479 U.S. 388, 403-06 (1987) (applying *Chevron* to OCC's interpretation of federal banking laws).

1. Under *Chevron*, if "Congress has not directly addressed the precise question at issue, . . . a court may not substitute its own construction of a statutory provision for a reasonable interpretation made by the administrator of an agency." 467 U.S. at 843-44. Thus, if a "statute is silent or ambiguous with respect to the specific issue, [administrative] regulations are given controlling weight unless they are arbitrary, capricious, or manifestly contrary to the statute." *Id.* at 843-44.

In reviewing the construction of a statute by the OCC or another agency, a "court need not conclude that the agency's construction was the only one it permissibly could have adopted, . . . or even the reading the court would have reached if the question initially had arisen in a judicial proceeding." *Id.* at 843 n.11. Rather, the court must defer to the OCC's construction of the NBA as long as that interpretation is reasonable. *See Clarke* v. *Securities Indus. Ass'n*, 479 U.S. at 403-04.

As shown below, the Fifth Circuit violated these settled principles of judicial deference in overruling the OCC's reasonable construction of Sections 24 (Seventh) and 92 of the NBA to permit national banks to broker annuities. It plainly was within the OCC's province to determine that annuities are not "insurance" for purposes of Section 92, but rather are a form of financial investment instrument of the type that national banks have long sold pursuant to their power to engage in the "business of banking."

Nothing in the NBA or its legislative history indicates that Congress intended to prohibit national banks from brokering annuities. Sections 24 (Seventh) and 92 do not

refer to "annuities" or define the statutory terms "business of banking" or "insurance," and those provisions certainly do not manifest the "clear" intent required by *Chevron* for a court to override an administrative agency's determination. 467 U.S. at 842. On the contrary, the incidental powers clause of Section 24 (Seventh)—like the provision of the New York Banking Law upon which it is based—"does not consist of common words of clear import, and that clause is susceptible to differing interpretation." *NYSALU*, 83 N.Y.2d at 360, 632 N.E.2d at 879, 610 N.Y.S.2d at 473. In these circumstances, the Fifth Circuit erred in considering *de novo* matters that Congress had left to the special expertise of the OCC.

2. The Fifth Circuit's failure to follow *Chevron* threatens the OCC's expert administration of the NBA and the development of banking generally. Congress has specifically charged the OCC with the administration of the NBA, *see* 12 U.S.C. §§ 1, 21-216(a), and has left many parts of that regulatory scheme to the implementing regulations of the OCC and other bank regulators, which "maintain virtually a day-to-day surveillance of the American banking system." *United States* v. *Philadelphia Nat'l Bank*, 374 U.S. 321, 329 (1963). Certain aspects of this scheme, especially those enacted many years ago, require interpretation and, frequently, reinterpretation to account for changing financial and technological developments, as well as consumer needs and preferences.

Since the enactment of the NBA in 1864, significant evolution has occurred in commercial banking and in the financial services industries in general. There have been both a proliferation of, and a growing homogenization in, products offered to consumers. For example, there is now relatively little difference for consumers among the wide range of money market and various other financial investment instruments offered by banks, brokerage firms and mutual funds. National banks must be able to rely on OCC

regulations and interpretations in order to respond to the changing requirements of the increasingly competitive marketplace for financial products and services.

The decision below, if allowed to stand, would pave the way for courts to substitute willy-nilly their construction of the NBA for the reasoned interpretations of the OCC, even where the regulators' interpretation is supported by the statute's language and legislative history. Such an approach inevitably would result in piecemeal and inconsistent application and development of the federal banking laws. It also would threaten the ability of national banks to meet their customers' demand for new financial products and services.

II. THE GREAT WEIGHT OF AUTHORITY SUPPORTS THE OCC'S CONCLUSION THAT ANNUITIES ARE FINANCIAL INVESTMENT INSTRUMENTS, NOT INSURANCE.

There is no sustainable basis for the Fifth Circuit's ruling, based on its impermissible *de novo* review of the OCC's decision, that "[a]nnuities are certainly no less a 'general' type of insurance than land title insurance or automobile insurance." (14a). This erroneous determination is the basis for the Fifth Circuit's equally misplaced holdings (i) that "annuities have nothing to do with the primary business of banking," and (ii) that Section 92 bars national banks from brokering annuities. (13a-14a).

Although insurance companies first developed and offered annuities, they have long been "recognized as investments rather than as insurance." 1 JOHN A. APPLEMAN, INSURANCE LAW & PRACTICE § 84, at 295 (1981); *see* DAVID SHAPIRO & THOMAS F. STREIFF, ANNUITIES 7 (1992) (annuities "are primarily investment products"). As the New York Court of Appeals has recognized unequivocally, the "great weight of authority supports the position that annuities

are not insurance." *NYSALU*, 83 N.Y.2d at 363, 632 N.E.2d at 881, 610 N.Y.S.2d at 475.[4]

"Annuit[ies] and insurance are opposites." *Helvering* v. *Le Gierse*, 312 U.S. 531, 541 (1941). Purchasers of insurance seek to protect against financial loss in the event of some adverse occurrence: death, disability, catastrophes such as floods or fires, or various other events causing injury or property damage. They seek protection (insurance), not investment income; indeed, if the insured-against loss does not occur, the insured does not receive any return on his or her premiums. *Compare* BLACK'S LAW DICTIONARY 90 (6th ed. 1990) (annuities) *with id.* 802 (insurance).

In contrast, purchasers of annuities, as is the case for purchasers of other bank investment products, seek a long-term return in the form of payments over time and not protection against some loss. In making investment decisions, consumers compare the investment risk and return of annuities with those of other investments available from banks and other financial intermediaries. "Any risk that the prepayment [premium] would earn less than the amount paid to [the annuitant] as an annuity [is] an investment risk similar to the risk assumed by a bank; it [is] not an insurance risk." *Helvering* v. *Le Gierse*, 312 U.S. at 542; *see also SEC* v. *United Benefit Life Ins. Co.*, 387 U.S. 202, 207-08 (1967) ("In fixing the necessary premium [for an annuity] mortality experience is a subordinate factor and the planning problem

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[4] *See, e.g., In re Young*, 806 F.2d 1303, 1306 (5th Cir. 1987) (quoting *In re Howerton*, 21 Bankr. 621, 623 (N.D. Tex. 1982)) ("an annuity is essentially a form of investment"); *Prudential Ins. Co. of Am.* v. *Howell*, 29 N.J. 116, 148 A.2d 145, 148 (1959) ("The risks assumed under life insurance policies and under annuity contracts are diametric opposites."); *Daniel* v. *Life Ins. Co.*, 102 S.W.2d 256, 260 (Tex. Civ. App. 1937) (an annuity "is essentially a form of investment, and uniformly held to be purely such").

is to decide what interest and expense rates may be expected. There is some shifting of risk from the policyholder to insurer, but no pooling of risks among policyholders. In other words, the insurer is acting in a role similar to that of a savings institution.").

The Fifth Circuit's "finding" that annuities are general "insurance" conflicts with this authority and cannot be reconciled with *SEC* v. *Variable Annuity Life Insurance Co. of America*, 359 U.S. 65, 71-73 (1959) ("*VALIC I*"), where this Court held that variable annuities are securities that must be registered with the Securities and Exchange Commission and are *not* "insurance" products exempt from such registration under the McCarran-Ferguson Act, 15 U.S.C. §§ 1011-1015. As the Court emphasized, annuities do not involve "true underwriting of risks, the one earmark of insurance as it has commonly been conceived of in popular understanding and usage." *VALIC I*, 359 U.S. at 73 (footnote omitted).

In interpreting the Employee Retirement Income Security Act, this Court recently reaffirmed its holding in *VALIC I* that a variable annuity "is not an 'insurance policy' . . . because the contract's entire *investment* risk remains with the policyholder." *John Hancock Mut. Life Ins. Co.* v. *Harris Trust & Sav. Bank*, 114 S. Ct. 517, 527 (1993) (emphasis in original). *VALIC I* should similarly guide the Court in construing the NBA.

The Fifth Circuit broadly proscribed the brokerage by national banks of both variable and fixed annuities. (*See* 3a, 13a). Although referring to variable annuities, which comprise the bulk of annuities currently sold, the reasoning of *VALIC I* applies to fixed annuities as well. As the OCC determined, and the Fifth Circuit did not dispute, "[f]ixed annuities differ [from variable annuities] only in that [fixed annuities] offer a reduced level of risk, combining for the risk-averse investor the best aspects of both certificates of deposit and annuities." (39a-40a).

In addition, the Fifth Circuit erroneously focused solely on annuities for which the benefits are paid over the duration of the annuitant's life (a life income option). (*See* 12a, 27a). Most annuities pay benefits, however, for a specified period (a term certain option, *e.g.*, five, ten or fifteen years) or in a lump-sum distribution of the entire cash value of the annuity. *See* DAVID SHAPIRO & THOMAS F. STREIFF, *supra*, at 2-4 (describing types of annuities).[5]

The Fifth Circuit also leapt from the observation that "[a]ll fifty states currently regulate annuities under their insurance laws," to the erroneous conclusion that the brokerage of annuities is excluded from the business of banking. (11a, 13a). The brokerage of an investment is not removed from the business of banking merely because that investment is regulated by an agency other than the OCC, or is subject to laws other than the NBA.[6] If that were the case, then banks could not sell securities, which are regulated by the SEC under the federal securities laws, as well as by state regulators under state securities laws. In *VALIC I*, this Court rejected the notion that annuities must be deemed insurance for all purposes simply because the states regulate annuities

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[5] According to a study by the Society of Actuaries and Life Insurance Marketing Association, over the 12-year average life of an annuity, only 16.8 percent of annuity holders annuitize (*i.e.*, elect to receive payments for life); the overwhelming majority elects some other type of withdrawal such as full or partial repayment. *See Are Annuities Insurance or Investment Products?*, The Newsletter of the Bank-Insurance Industry, 1993-3, at 2-3 (published by Kenneth Kehrer Assocs., Princeton, N.J.).

[6] "'Banking' and 'insurance' are not mutually exclusive businesses; 'from a functional point of view there is a considerable overlap between the [two].'" *American Ins. Ass'n* v. *Clarke*, 656 F. Supp. 404, 409-10 (D.D.C. 1987), *aff'd*, 865 F.2d 278 (D.C. Cir. 1988) (quoting HENRY HARFIELD, BANK CREDIT AND ACCEPTANCES 184 (5th ed. 1974)) (brackets in original).

as insurance for certain purposes. The Court held that the "meaning" of "insurance or annuity" under federal statutes "is a federal question," and that "how states might have ruled is not decisive." 359 U.S. at 69.[7]

In addition, the Fifth Circuit ignored the OCC's reasonable conclusion that annuities resemble securities that banks are specifically authorized to sell to their customers. (*See* 37a-38a). Section 24 (Seventh) expressly provides that national banks may "purchas[e] and sell[] securities and stock without recourse, solely upon the order, and for the account of, customers," and, as is shown below, banks have historically sold securities to their customers.

The OCC also reasonably determined that annuities "functionally" resemble certificates of deposit that banks routinely offer to their customers. (40a-41a). The similarity between these two financial investment instruments is such that "the annuity is now the favorite alternative to the CD." DAVID SHAPIRO & THOMAS F. STREIFF, *supra*, at 8. Aside from their power to conduct the "business of banking," national banks may also sell these investment instruments because of the express authorization in Section 24 (Seventh) for such banks to "receiv[e] deposits."

In sum, the OCC had far more than the reasonable basis that is necessary under *Chevron* for its determination that, for purposes of the federal banking laws, annuities are financial investment instruments, not general insurance.

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[7] As is discussed below, however, because the "incidental powers" clause of Section 24 (Seventh) was taken virtually verbatim from early bank legislation in New York, interpretations of the corollary provision of New York law are persuasive—if not dispositive—here. *See*, *infra*, at 16-19.

III. SECTION 24 (SEVENTH) AUTHORIZES NATIONAL BANKS TO ENGAGE IN ALL ASPECTS OF THE "BUSINESS OF BANKING," INCLUDING THE BROKERAGE OF ANNUITIES AND OTHER FINANCIAL INVESTMENT INSTRUMENTS.

Having erroneously determined that annuities are a form of "general" insurance, the court below compounded its error under *Chevron* by disregarding the OCC's considered construction of the incidental powers clause of Section 24 (Seventh). Without providing any explication of the meaning of Section 24 (Seventh) or any delineation of the scope of the "business of banking," the court concluded that "conceding arguendo that the power to sell annuities would be one incidental to banking, by no stretch of the imagination can that power be deemed necessary." (15a). The court erroneously construed the word "necessary" to require that an activity be essential—or "intimately related to the bank's primary business of lending"—to be permissible under Section 24 (Seventh). (14a).

Whether an activity is "necessary" to the "business of banking" under Section 24 (Seventh) does not, as the Fifth Circuit held, depend upon whether that activity is characterized by some general label, such as "insurance" or "banking," or is otherwise essential to "lending."[8] Rather, as the OCC determined (38a (citing OCC Interpretive Letter No. 494, *reprinted in* [1989-1990 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,083, at 71,194-71,201 (Dec.

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[8] Lending is, of course, only one aspect of the business of banking. In any event, labeling is no substitute for analysis in construing the NBA. *See American Ins. Ass'n* v. *Clarke*, 656 F. Supp. at 408 ("there can be no serious quarrel with the [OCC's] assertion that it is entitled to look beyond the label given a certain activity to determine whether or not it is permissible").

20, 1989) ("Interpretive Letter No. 494")),[9] the inquiry must focus on whether the activity is consistent with the historic function of banks as financial intermediaries.

A. The Language and Legislative History of the NBA Support the OCC's Interpretation of the "Business of Banking."

1. By its terms, Section 24 (Seventh) authorizes national banks to engage in all aspects of the business of banking. While the statute identifies five specific powers that are granted to national banks, it also *expressly* authorizes those banks to exercise "all such incidental powers as shall be necessary to carry on the business of banking."[10] It is a settled rule of construction that "a court should 'give effect, if possible, to every clause and word of a statute.'" *Moskal* v. *United States*, 498 U.S. 103, 109-110 (1990); *see* 2A SUTHERLAND ON STATUTORY CONSTRUCTION § 46.06, at

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[9] The OCC's determination that national banks may broker fixed annuities incorporated the reasoning of its earlier interpretive letter, which had permitted such banks to "broker a wide variety of financial investment instruments," such as agricultural, oil and metals futures. (*See* 38a).

[10] Section 24 (Seventh) provides that national banks may exercise "*all such incidental powers as shall be necessary to carry on the business of banking*; by discounting and negotiating promissory notes, drafts, bills of exchange, and other evidences of debt; by receiving deposits; by buying and selling exchange, coin and bullion; by loaning money on personal security; and by obtaining, issuing, and circulating notes according to the provisions of title 62 of the Revised Statutes. The business of dealing in securities and stock by the association shall be limited to purchasing and selling such securities and stock without recourse, solely upon the order, and for the account of, customers, and in no case for its own account, and the association shall not underwrite any issue of securities or stock . . . ." (Emphasis added)

119-20 (5th ed. 1992) ("A statute should be construed so that effect is given to all of its provisions, so that no part will be inoperative or superfluous, void or insignificant. . . .") (footnotes omitted). In order to give full effect to all of the language of Section 24 (Seventh), it is necessary to construe the five enumerated powers as archetypes or examples of banking powers and not as the exclusive list.

If the Fifth Circuit's interpretation of Section 24 (Seventh) were correct, Congress would not have included the term "business of banking" in the NBA, because it would have been superfluous. Instead, Congress would have confined Section 24 (Seventh) to the enumerated powers and incidental powers necessary to carry out those enumerated powers. By expressly authorizing national banks to carry on the broadly-phrased "business of banking," rather than just the specifically-enumerated powers and activities incidental to those powers, Congress plainly expressed its intent to authorize banks to engage in the full panoply of activities that are necessary for banks to fulfill their function as financial intermediaries. This authorization includes those activities that would develop in response to inevitable changes in the financial world and the public's demand for banking services.

2. The OCC's interpretation of the incidental powers clause as not being confined to the specifically enumerated powers in Section 24 is consistent with the origins and history of the NBA, including the contemporaneous construction of the New York law upon which the NBA was patterned.

The NBA replaced the National Currency Act, which had been enacted a year earlier in 1863. Congress passed these measures to induce state-chartered banks to convert to federal charters in order to promote the development of a national currency and banking system. *See* BRAY HAMMOND, BANKS AND POLITICS IN AMERICA 724-27 (1957). During the first half of the nineteenth century, bank regulation was almost exclusively the province of the states. *See* Edward

Symons, *The "Business of Banking" in Historical Perspective*, 51 GEO. WASH. L. REV. 676, 688-89 (1983).

Accordingly, Congress looked to state law—and particularly New York law—in formulating the powers of national banks. Congress adopted the "incidental powers" clause of Section 24 (Seventh) nearly verbatim from the New York Free Banking Act of 1838, *see Arnold Tours, Inc.* v. *Camp*, 472 F.2d 427, 431 (1st Cir. 1972), and the legislative history indicates that Congress sought to confer upon national banks *all* of the powers then possessed by New York banks to carry on the business of banking.[11] "When a statute is [copied] from another, even a foreign, State, it generally is presumed to be adopted with the construction which it has received." *James* v. *Appel*, 192 U.S. 129, 135 (1904) (Holmes, J.); *see* 2B SUTHERLAND ON STATUTORY CONSTRUCTION § 52.02, at 198 (5th ed. 1992) ("courts of the adopting state usually adopt the construction placed on the statute in the jurisdiction in which it originated").

The incorporation of New York law included the judicial construction of that law prevailing at the time of the enactment of the NBA, most especially the decision in *Curtis* v. *Leavitt*, 15 N.Y. 9 (1857), which is considered the seminal decision on the meaning of the statutory term "business of

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[11] The Currency Act's principal draftsman, Representative Spaulding, explained that "[t]he bill in all its essential features is like the free banking law of the State of New York, which has been in successful operation in that State since 1838," and that it is intended "to nationalize the banking system of New York." CONG. GLOBE, 37th Cong., 3d Sess. 1114, 1141 (1863). Similarly, Representative Baker stated: "I would like to see all the States of the Union adopt the free banking system of the State of New York in its present completeness and perfection." *Id.* at 1142.

banking" under New York and federal law.[12] This Court, and lower federal courts, have thus relied on *Curtis* in construing the NBA.[13] The OCC similarly relied on *Curtis*, which the court below ignored in its decision, in determining that national banks may broker annuities. (*See* Interpretive Letter No. 494 at 71,196).

In *Curtis*, the New York Court of Appeals held that the incidental powers clause of the New York Free Banking Act did not limit the power of banks to the specifically enumerated powers, but, instead, authorized the inclusion of other banking activities as they developed over time. *See* 15 N.Y. at 58 (Comstock, J.) ("Those specifications were evidently intended not to restrict the appropriate business of banking, but as a mere legislative definition of that business."). As Judge Brown explained in a concurring opinion:

> The implied powers [of a bank] exist by virtue of the grant [to do the business of banking], and are not enumerated and defined; because no human sagacity can foresee what implied powers may, in the progress of time, the discovery and perfection of better methods of business, and the ever-varying attitude of human relations, be required to give

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[12] *See, e.g.*, Edward Symons, *supra*, at 694-98; Ralph F. Huck, *What Is the Banking Business?*, 21 BUS. LAW. 537, 540-42 (1966); Phillip R. Trimble, *The Implied Power of National Banks to Issue Letters of Credit and Accept Bills*, 58 YALE L.J. 713, 718 (1949); Henry Harfield, *The National Bank Act and Foreign Trade Practices*, 61 HARV. L. REV. 782, 798-99 (1948).

[13] *See, e.g.*, *Auten* v. *United States Nat'l Bank*, 174 U.S. 125, 143 (1899); *Arnold Tours, Inc.* v. *Camp*, 472 F.2d at 431; *Sneeden* v. *City of Marion*, 64 F.2d 721, 724 (7th Cir. 1933); *Kirkman* v. *Farmers' Sav. Bank*, 28 F.2d 857, 861 (8th Cir. 1928).

> effect to the express powers. They are, therefore, left to implication.

Id. at 157.[14]

The New York Court of Appeals later reaffirmed the need to construe the state's banking law to meet the changing demands of the business of banking. In *Dyer* v. *Broadway Central Park*, 252 N.Y. 430, 169 N.E. 635 (1930), for example, the court rejected the argument that all contracts by banks to purchase securities on behalf of their customers were *ultra vires*, stating: "Banks *ex necessitate* have been required to extend their functions and perform services formerly foreign to the banking business. Courts have taken cognizance of that fact in passing upon cases involving questions of banking law." *Id.* at 433, 169 N.E. at 636. The court cautioned that "care should be exercised not to cripple [banks] and break down their usefulness by a narrow and unreasonable construction of the statutes which will result in unwisely limiting their usefulness in the transaction of business under modern conditions." *Id.* at 434, 169 N.E. at 636.

Relying on *Curtis* and its progeny, the New York Court of Appeals recently confirmed that the incidental powers clause of the New York Banking Law empowers state-

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[14] *Curtis* squarely rejected the even more extreme notion, which the Fifth Circuit adopted (15a), that the inclusion in the incidental powers clause of the term "necessary" limits banks to the exercise of only those incidental powers that are *essential* to the exercise of specifically enumerated powers: "But necessity is a word of flexible meaning. There may be an absolute necessity, a great necessity, and a small necessity; and between these degrees there may be many others depending on the ever varying exigencies of human affairs." *Curtis*, 15 N.Y. at 64 (Comstock, J.); *see also McCulloch* v. *Maryland*, 17 U.S. (4 Wheaton) 316, 413-15 (1819) (the term "necessary" "frequently imports no more than that one thing is convenient, or useful, or essential to another").

chartered banks to adapt their product lines to meet changing economic conditions and the evolving demands of commercial banking customers: "the clause must be construed as an independent, express grant of power, intended to reflect the ever-changing demands of the banking business." *See NYSALU*, 83 N.Y.2d at 363, 632 N.E.2d at 881, 610 N.Y.S.2d at 475. Based on this conclusion and principles of judicial deference similar to those articulated in *Chevron*, the Court of Appeals held that it was not unreasonable for the New York Banking Department to have determined that New York-chartered banks may broker annuities because annuities are financial investment instruments of the type that banks have historically been permitted to sell. *Id.* at 364, 632 N.E.2d at 882, 610 N.Y.S.2d at 476.

The approach in *NYSALU* rests on the same principles that Congress incorporated into the NBA and, thus, is far more in keeping with Congress's intent in enacting Section 24 (Seventh) than is the Fifth Circuit's restrictive interpretation of the incidental powers clause.

B. This Court's Decisions Support the OCC's Construction of the "Business of Banking."

This Court has consistently given full effect to the language of the incidental powers clause of Section 24 (Seventh) and has authorized national banks to exercise powers that are not limited to those that are essential to the performance of one of the enumerated powers.[15] For

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[15] *See, e.g., Franklin Nat'l Bank* v. *New York*, 347 U.S. 373, 377 (1954) ("business of banking" includes power to advertise bank services); *Colorado Nat'l Bank* v. *Bedford*, 310 U.S. 41, 48-50 (1940) (conduct safe-deposit business); *First Nat'l Bank* v. *City of Hartford*, 273 U.S. 548, 559-60 (1927) (sell and deal in mortgages and other evidences of debt); *Clement Nat'l Bank* v. *Vermont*, 231 U.S. 120, 140 (1913) (pay taxes on behalf of depositors); *Miller* v.

(continued...)

example, in *First National Bank* v. *National Exchange Bank*, 92 U.S. 122 (1875), one of its earliest decisions interpreting Section 24 (Seventh), this Court rejected the notion that the "incidental" powers of national banks are limited to those that are necessary to the performance of the specifically enumerated powers: "These powers are such as are required to meet *all the legitimate demands of the authorized business*, and to enable a bank to conduct its affairs, within the general scope of its charter, safely and prudently. This necessarily implies the right of a bank to incur liabilities in the regular course of its business, as well as to become the creditor of others." *Id.* at 127 (emphasis added). *See also Miller* v. *King*, 223 U.S. 505, 511 (1912) (collecting judgment on behalf of depositor is not "so disconnected with the banking business as to make it in violation of" Section 24 (Seventh)); *Logan County Nat'l Bank* v. *Townsend*, 139 U.S. 67, 73 (1891) (national bank possesses "such incidental powers as are necessary to carry on the business of banking for which it was established").

Moreover, this Court's decisions confirm that the incidental powers clause authorizes national banks, consistent with their function as financial intermediaries, to engage in those activities that have "grown out of the business needs of the country." *Merchants' Bank* v. *State Bank*, 77 U.S. (10 Wallace) 604, 648 (1871) (power to certify checks); *see also Colorado National Bank*, 310 U.S. 41, 49-50 (1940) ("national banks do and for many years have carried on a safe-deposit business," and "such a generally adopted method

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[15](...continued)
King, 223 U.S. 505, 511 (1912) (collect judgment on behalf of depositor); *Wyman* v. *Wallace*, 201 U.S. 230, 243 (1906) (borrow money). Although the OCC expressly relied upon these decisions in permitting national banks to broker financial investment instruments, *see* Interpretive Letter No. 494 at 71,196-71,197, the court below did not mention, much less reconcile, this authority.

of safeguarding valuables must be considered a banking function authorized by Congress"); *Clement Nat'l Bank* v. *Vermont*, 231 U.S. 120, 140 (1913) (paying taxes on behalf of depositors "promote[s] the convenience of [the bank's] business").

The Court's most recent decision construing the incidental powers clause, *Franklin National Bank* v. *New York*, 347 U.S. 373 (1954), makes clear that Congress has authorized national banks to fulfill their role as financial intermediaries by meeting the "modern" requirements of the business of banking. In holding that national banks could advertise their services, the Court eschewed the static interpretation of "necessary" adopted by the Fifth Circuit below, instead requiring only that the activity be "usual and useful" to modern banking:

> *Modern competition for business finds advertising one of the most usual and useful of weapons.* We cannot believe that the incidental powers granted to national banks should be construed so narrowly as to preclude the use of advertising in any branch of their authorized business.

Id. at 377 (emphasis added).

The Fifth Circuit's construction of the incidental powers clause of Section 24 (Seventh) also conflicts with that of the other courts of appeals. *See First Nat'l Bank* v. *Taylor*, 907 F.2d 775, 778 (8th Cir.) (collecting cases holding that "the 'incidental powers' of national banks are not limited to activities that are deemed essential to the exercise of express powers"), *cert. denied*, 498 U.S. 972 (1990). The Ninth Circuit, for example, has emphasized that the NBA "did not freeze the practices of national banks in their nineteenth century forms," and that the incidental powers clause "permit[s] the use of new ways of conducting the very old business of banking." *M&M Leasing Corp.* v. *Seattle First Nat'l Bank*, 563 F.2d 1377, 1382 (9th Cir. 1977), *cert.*

denied, 436 U.S. 956 (1978). The Fifth Circuit below completely ignored this authority.

This Court should now reaffirm that the incidental powers clause constitutes, as the OCC determined, an *express* grant of authority to national banks—separate and apart from the five other express powers—to engage in such activities as are necessary "to meet all the legitimate demands" of the "business of banking" as that business evolves to serve the changing needs of our dynamic economy and society. Even if the Court discerns any ambiguity on this point, and it should not, *Chevron* requires that the OCC's entirely reasonable construction of the clause to that effect be sustained.

C. The Brokerage of Financial Investment Instruments, Including Annuities, Is Part of the "Business of Banking."

In authorizing national banks to broker annuities, the OCC relied on its prior determination that such banks "may broker a wide variety of financial investment instruments." (*See* 38a). That decision, in turn, was based on (i) the settled power of banks, as part of the "business of banking," to broker "a wide variety of financial, investment, and monetary instruments and other financial commodities," and (ii) the express provisions in Section 24 (Seventh) permitting banks to broker securities and to extend credit. *See* Interpretive Letter No. 494 at 71,199-71,201. The OCC's determination properly reflects the historic role of banks as financial intermediaries and correctly construes Section 24 (Seventh) to permit banks to offer new financial products, such as annuities, which their customers demand.

The business of banking is one of financial intermediation. As this Court has recognized, "[t]he very object of banking is to aid the operation of the laws of commerce by serving as a channel for carrying money from

place to place," *Auten* v. *United States Nat'l Bank*, 174 U.S. at 143 (citing *Curtis* v. *Leavitt*, 16 N.Y. 9 (1857)), and banks are "the intermediaries in most financial transactions." *Philadelphia Nat'l Bank*, 374 U.S. at 326; *see also Delaware* v. *New York*, 113 S. Ct. 1550, 1554 (1993) ("in the modern financial services industry," banks serve as "financial intermediaries" in the "clearing[]" of "securities transactions"); *Auten*, 174 U.S. at 142 (quoting GILBART ON BANKING, vol. 1, p. 2) (a banker is "a dealer in capital"); *Block* v. *Pennsylvania Exch. Bank*, 253 N.Y. 227, 230-31, 170 N.E. 900, 901 (1930) (Cardozo, J.) ("The central function of a commercial bank is to substitute its own credit, which has general acceptance in the business community, for the individual's credit, which has only limited acceptability. . . . Whatever is an appropriate and usual incident to this substitution or exchange of credits, instead of being foreign to the functions and activities of banking, is in truth of their very essence.").

Banks serve as financial intermediaries both as principals and as agents. As principals, banks receive deposits from certain customers and extend credit to other customers. As agents, banks sell financial investment instruments and obligations, including loans, deposits, commercial paper, bonds, stocks and futures, issued by other parties to bank customers. Not all of these instruments and obligations were in existence at the time of the enactment of the NBA; many grew out of the changing requirements of bank customers and the economy. Annuities are simply another such financial investment instrument.

The court below completely ignored that banks "long have arranged the purchase and sale of securities as an accommodation to their customers." *Securities Indus. Ass'n* v. *Board of Governors*, 468 U.S. 207, 215 (1984). "Congress expressly endorsed this traditional banking service" in enacting the Glass-Steagall Act and, thus, approved in Section 24 (Seventh) the power of banks to

broker securities for their customers "'to the same extent as heretofore.'" *Id.* at 215 & n.13 (quoting S. Rep. No. 77, 73d Cong., 1st Sess. 16 (1933)). The fact that the incidental powers clause authorized national banks to broker securities prior to the passage of the Glass-Steagall Act makes clear that such banks possessed the power to broker other financial investment instruments as well.

The power of commercial banks to broker securities—and, by extension, other forms of financial investment instruments—was so well established that in 1930 then-Chief Judge Cardozo of the New York Court of Appeals recognized that "[t]here is no question that the practice of banking as it has developed in our day" includes the brokerage of securities, and indeed, that "[t]he practice is so general that it may be the subject of judicial notice." *Block*, 253 N.Y. at 232, 170 N.E. at 901-02. Construing the New York Banking Law, the court did not confine the "business of banking" to the specific activities previously performed by commercial banks. Rather, "the [c]ourt acknowledged that the development and the evolution of business must be considered." *NYSALU*, 83 N.Y.2d at 362, 632 N.E.2d at 880, 610 N.Y.S.2d at 474 (explaining *Block*).

The New York Court of Appeals recently relied upon *Block*, and its focus on the function of banks as financial intermediaries, in approving the brokerage of annuities by New York-chartered banks. *See NYSALU*, 83 N.Y.2d at 362, 632 N.E.2d at 880, 610 N.Y.S.2d at 475 (quoting *Block*, 253 N.Y. at 232, 170 N.E. at 901) ("the test of a bank's power to undertake certain activities 'is the relation of the act to that substitution of credits which is of the essence of the banking function'"). The court stressed that "State-chartered commercial banks commonly broker other financial investment instruments, including certificates of deposit and various types of securities, which closely resemble annuities." *Id.* at 364, 632 N.E.2d at 882, 610 N.Y.S.2d at 476.

Because the brokerage of financial investment instruments has historically been performed by, and is one of the functions of, national banks, the OCC reasonably determined that the brokerage of annuities is part of the "business of banking."

D. The Brokerage of Annuities by National Banks Is Supported by Sound Banking Policy.

In construing the scope of the "business of banking" powers of national banks, this Court has taken into account the impact of a particular activity on bank safety and soundness. *See, e.g., Awotin* v. *Atlas Exch. Nat'l Bank*, 295 U.S. 209, 214 (1935) ("purpose and effect of the [NBA] is to protect their depositors and stockholders and the public from the hazards of contingent liabilities"); *Texas & Pac. Ry.* v. *Pottorff*, 291 U.S. 242 (1934) (national bank's pledge of its assets to secure deposit "contrary to good banking practice"); *First Nat'l Bank* v. *Converse*, 200 U.S. 425, 439 (1906) (national bank may not "engage in or promote a purely speculative business or adventure").

There is no evidence that permitting national banks to broker annuities would jeopardize their safety and soundness. Because national banks act only as agents for the sale of annuities—and not as the issuer—they incur no principal risk, no interest rate risk, and no actuarial risk. On the contrary, barring national banks from the brokerage of annuities would place national banks at a competitive disadvantage vis-a-vis New York-chartered banks (and banks chartered by other States that follow the New York approach) and other financial intermediaries (including brokerage and insurance companies with bank affiliates) that possess the power to broker annuities. The existence of such fundamental differences in the powers of national and state-chartered banks is contrary to Congress's intent in enacting the NBA and would sharply devalue the charters of national banks by retarding necessary innovation by those banks.

In any event, *Chevron* required the lower court to defer to the OCC's determination that the brokerage of annuities by national banks (i) is a "logical complement to other financial services [banks] offer[]," such as investment advice and discount brokerage services, (ii) "will provide a valuable additional source of income and will help [such banks] compete effectively with other providers of financial services," and (iii) will "benefit" consumers by "increas[ing the] range of products made available" to them. (47a-48a).

* * *

The foregoing considerations establish that Section 24 (Seventh) authorizes national banks to broker annuities and dispel any notion that Congress has legislated to the contrary. Even if these considerations were less definitive, the Fifth Circuit had no basis to substitute its own views for the reasonable interpretation of the OCC. Under *Chevron*, absent "clear" evidence of congressional intent to bar the brokerage of annuities, *Chevron*, 467 U.S. at 842, the Fifth Circuit was required to defer to the OCC.

IV. Section 92 Does Not Limit The "Business Of Banking" Powers Of National Banks.

Having erroneously concluded that annuities are a form of "insurance" (10a), the Fifth Circuit compounded its error under *Chevron* by holding that Section 92 bars national banks in communities of more than 5,000 persons from acting as sales agents for *all* "insurance" products, even those that *are* incidental to the business of banking. (*See* 14a-17a). This conclusion conflicts with Section 92's language and legislative history, which, as the OCC determined (42a-43a), demonstrate that that provision is a supplemental grant of authority to banks in small towns to engage in insurance-

related activities that are not within the business of banking.[16]

Although acknowledging its obligation under *Chevron* (8a-9a), the Fifth Circuit nonetheless rejected the OCC's position, reasoning that Section 92 "exhibits Congress' clear intent to permit only banks in towns of less than 5,000 inhabitants to sell insurance products." (9a). The Fifth Circuit first ignored the explicit statement in Section 92 that the powers conferred by that section were "*[i]n addition* to the powers now vested by law in national banking associations," 12 U.S.C. § 92 (emphasis added). This is an unequivocal statement that Section 92 imposes no limits on powers granted, by Section 24 (Seventh) or otherwise, to national banks but only supplements those powers. *See Independent Bankers Ass'n of Am.* v. *Heimann*, 613 F.2d. 1164, 1170 n.18 (D.C. Cir. 1979), *cert. denied*, 449 U.S. 823 (1980). In addition, Section 92's legislative history indicates that "Congress was concerned only with providing small-town banks with an additional profit source, not with prohibiting city banks from selling insurance." *Independent*

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[16] Section 92 provides:

"*In addition to the powers now vested by law in national banking associations* organized under the laws of the United States any such association located and doing business in any place the population of which does not exceed five thousand inhabitants, . . . may, under such rules and regulations as may be prescribed by the [OCC], act as the agent for *any fire, life, or other insurance company* authorized by the authorities of the State in which said bank is located to do business in said State, by soliciting and selling insurance and collecting premiums on policies issued by such company; and may receive for services so rendered such fees between the said association and the insurance company for which it may act as agent." (Emphasis added).

Ins. Agents of Am., Inc. v. *Board of Governors*, 736 F.2d 468, 477 n.6 (8th Cir. 1984).[17]

The court below then attempted to support its strained construction of Section 92 by relying on its prior decision in *Saxon* v. *Georgia Association of Independent Insurance Agents*, 399 F.2d 1010 (5th Cir. 1968), rendered sixteen years before this Court's decision in *Chevron*. (6a, 16a-17a). In *Saxon*, the Fifth Circuit did not defer to the OCC's interpretation of Section 92 (as is now required by *Chevron*), but instead misapplied the maxim of construction *expressio unius est exclusio alterius* to conclude that Section 92 implicitly bars national banks located outside of small towns from operating a general life and casualty insurance agency. 399 F.2d at 1013-14.

The Fifth Circuit's continued reliance upon the maxim of *expressio unius* was entirely misplaced. (*See* 15a-16a). Even if it had been proper to apply this maxim in construing Section 92, that analysis could have at most demonstrated that the statute impliedly bars national banks in towns of more than 5,000 persons from engaging in general insurance activities if such activities are *not* incidental to the business of banking. Section 92 does not address—and, thus, the maxim cannot be invoked to restrict—the powers granted to national banks by Section 24 (Seventh) to engage in insurance-related activities that *are* incidental to the business of banking. *Cf. Springer* v. *Government of the Philippine Islands*, 277 U.S. 189, 206 (1928) (maxim of *expressio unius*

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[17] Section 92's sponsor, Senator Owen, described this provision as "giving some additional powers to the small banks to act as agents in insurance matters." 53 CONG. REC. 11,002 (1916); *see also* 53 CONG. REC. 11,001 (1916) (OCC statement that Section 92 was based on consideration of "how the powers of these small national banks might be enlarged").

"must yield whenever a contrary intention on the part of the law-maker is apparent").

Moreover, the OCC's determination that Section 92 applies only to the activities of national banks acting as agents for "general" forms of insurance, such as "fire" and "life" insurance, is supported by the principle *ejusdem generis*—a general term in a statutory list "should be understood in light of the specific terms that surround it." *Hughey* v. *United States*, 495 U.S. 411, 419 (1990). Under the Fifth Circuit's expansive reading of Section 92, the statutory terms "fire" and "life" insurance would be mere surplusage, because all forms of insurance are included in the phrase "any . . . insurance company." In contrast, the OCC's interpretation gives effect to each word of the statute, by reading Section 92 as addressing only the general forms of insurance enumerated in the provision.

Contrary to *Chevron*, the panel below rejected the OCC's determination even though the OCC's position is consistent with the decisions of two other courts of appeals. *See Independent Bankers Ass'n* v. *Heimann*, 613 F.2d at 1170 (upholding the OCC's ruling that national banks outside of small towns could sell credit life insurance); *Independent Ins. Agents* v. *Board of Governors*, 736 F.2d at 477 n.6 (upholding Federal Reserve's approval of application to engage in credit-related property and casualty insurance, and noting "strong argument" that *Saxon* was "wrongly decided"). This conflict demonstrates that the statute does not clearly evince Congress's intent to bar banks from brokering annuities. On the contrary, these decisions confirm, at the least, that the OCC had a reasonable basis for its determination that Section 92 should not be read to have that effect.

CONCLUSION

The judgment below should be reversed.

Respectfully submitted,

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July 29, 1994